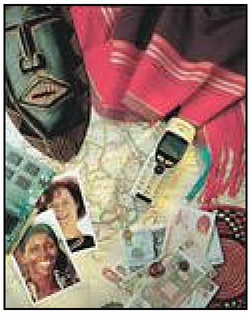

FINANCE & DEVELOPMENT
A quarterly magazine of the IMF
December 2001, Volume 38, Number 4

The Need for Stronger Domestic Policies and International Support

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Globalization, or the increasing economic integration among nations, has accelerated sharply over the past half century, driven largely by the remarkable expansion of international trade and capital flows, as well as by the extraordinary advances in information and communication technologies. As this process has grown in intensity, it has brought great benefits in terms of worldwide economic and social development, as evidenced by unprecedented growth in global output and real per capita income and, more generally, by major improvements in human welfare.

These benefits have not been evenly distributed, however, and income disparities between rich and poor countries, as well as within many countries, have increased. Today, out of the world's 6 billion people, some 2.8 billion—or almost one-half—still live on less than $2 a day, and 1.2 billion—or one-fifth—live on less than $1 a day. The persistence of abject poverty and other problems, including those posed by the volatility of international capital flows, have been a matter of serious concern. But this does not imply that the growing openness of the world economy is the cause of income inequality and financial instability. Although it is not an entirely benign phenomenon, globalization is a powerful engine of world prosperity, and it is certainly here to stay. The basic issue is what policies and reforms are most likely to bring about sustainable economic growth for the benefit of all the peoples of the world.

Since the early 1970s, some developing countries, notably in East Asia, have made substantial progress in closing the income gap relative to the advanced economies. But in many other countries, progress has been slow, and, in still others, the gap has continued to grow. In sub-Saharan Africa, the income gap relative to the advanced economies has widened and per capita incomes in a number of countries have actually dropped, in absolute terms. There has also been an erosion of sub-Saharan Africa's share of world trade, even for its traditional commodity exports, while foreign direct investment in the region has generally remained at very low levels.

Thus, sub-Saharan Africa entered the new millennium trailing well behind other regions and facing enormous development challenges. Average real per capita income, saving, and investment are all roughly unchanged today relative to their 1970 levels. Although education and health services have improved appreciably in some countries, social conditions in sub-Saharan Africa are among the poorest in the world (see table). What is much more worrisome is that HIV/AIDS has assumed alarming proportions in an increasing number of African countries, shattering lives and posing a major threat to future economic growth and development.

Causes of inadequate growth

The basic question often asked, therefore, is why has sub-Saharan Africa's growth lagged behind that of other regions since the early 1970s? Extensive research and analysis both within and outside Africa have often highlighted the following causes:

- adverse geographic and demographic conditions;
- terms of trade and other external shocks;
- macroeconomic policy weaknesses, particularly inappropriate fiscal policies;
- structural policy failures;
- weaknesses in governance, notably poor management of financial resources stemming from the production and export of major agricultural commodities, minerals, and oil; and
- political instability and conflicts.

Adverse geographic and demographic factors, as well as terms of trade shocks, which are largely beyond the control of the authorities, have certainly affected the performance of many African countries, especially the poorest ones. But homegrown factors and policies have been even more of an impediment to the development of the right conditions for investment and growth.

In the 1970s and much of the 1980s, most African countries sought to achieve economic and social progress through government controls on prices, interest rates, and exchange rates, as well as restrictions on various aspects of production, distribution, and trade. At the same time, despite deteriorating terms of trade, they pursued expansionary fiscal and monetary policies, relying increasingly on domestic and foreign borrowing to finance large budgetary and public enterprise deficits. As a result, the entire incentive structure was seriously damaged, investment choices were distorted, and essential social services were neglected, while corruption spread, competitiveness weakened, and the external debt became unsustainable. These problems were exacerbated by political instability and conflicts, further eroding investor confidence and reinforcing perceptions of the region as the riskiest in the world. For a long time, most African countries resisted adopting the market-oriented policies and reforms needed to reap the benefits of globalization, and, consequently, their economies stagnated or declined and poverty increased.

Selected social indicators of low- and middle-income countries

	Population living on less than $1 a day (percent)		Adult illiteracy rate (percent)	Life expectancy at birth (years)	Infant mortality rate (per 1,000)	HIV prevalence (percent of adults ages 15-49)
	1990	1998	1999	1999	1999	1999
East Asia and Pacific	27.6	14.7	15	69	35	0.22
Eastern Europe and Central Asia	1.6	3.7	3	69	21	0.18
Latin America and Caribbean	16.8	12.1	12	70	30	0.58
Middle East and North Africa	2.4	2.1	36	68	44	0.03
South Asia	44.0	40.0	46	63	74	0.56
Sub-Saharan Africa	47.7	48.1	39	47	92	8.38
All regions	29.0	23.4	25	64	59	1.19

Sources: World Bank, 2001, *Global Economic Prospects and the Developing Countries* (Washington); and World Bank, 2001, *World Development Indicators* (Washington).

Recent progress and development goals

As African countries have begun to address these problems, for the first time in a generation, there are now signs of progress in the region. Apart from those countries that have been pursuing sound policies for over a decade (notably Botswana, Mauritius, and Uganda), in a growing number of other countries (including Benin, Burkina Faso, Mozambique, Senegal, and Tanzania), there has been a major turnaround in the policy environment, leading to a significant increase in the growth of output and real per capita income, as well as an improvement in some social indicators.

Nonetheless, sub-Saharan Africa has a long way to go to make up for the ground lost over the past three decades so that it can begin to catch up with other developing countries. In particular, the region's current overall performance is well below what is required to achieve the international development goals for poverty reduction, education, health, gender equality, and environmental sustainability by the target dates—in most cases, 2015. (These goals, together with a call for a global partnership for development, have recently been reemphasized and incorporated in the United Nations' Road Map Towards the Implementation of the Millennium Declaration, which was adopted in September 2000 by 147 heads of state or government.) To reach these goals, especially the goal of reducing the proportion of people living in extreme poverty (or on less than $1 a day) by one-half between 1990 and 2015, sub-Saharan African countries will have to raise their real GDP growth rate to 7-8 percent a year on a sustained basis, or roughly twice the rate recorded in the second half of the 1990s. It will be particularly important for Africa's largest economies—Nigeria and South Africa—to achieve robust growth to facilitate and enhance the growth prospects of the region as a whole.

The fundamental challenge facing African countries, therefore, is how to ensure faster economic growth and poverty reduction in the context of an increasingly interdependent world. Although there is no simple, universal blueprint for a successful development strategy, policymakers do know a lot about the elements of sustainable growth with equity and social justice. Empirical studies indicate that, in general, such growth requires increasing investment, especially by promoting private initiative; enhancing human resource development; and improving overall economic efficiency and productivity. But ultimately, each sub-Saharan African country will have to formulate its own development strategy with a comprehensive program of action that best suits its specific circumstances. Moreover, to be effective, the country strategy will need to be based on an open, transparent, and participatory approach that ensures broad national ownership of the desired goals and the direction of policies and measures.

Therefore, the mix as well as the sequencing of economic and social policies and reforms will necessarily vary across sub-Saharan Africa. However, in view of the record and experience so far, African countries will need to strengthen their macroeconomic policies and structural reforms if they are to maximize the gains from globalization, accelerate growth, and reduce poverty. This message has been gaining ground in recent years under the impetus of a number of African action programs, which have now been merged into the New African Initiative. Importantly, this initiative is firmly anchored in the principles of African ownership, leadership, and commitment to the implementation of strong domestic policies and reforms. But, to be successful, Africa's reform programs will need to be coupled with increased and better-coordinated international technical and financial assistance.

Strengthening macroeconomic policies

In light of the circumstances and objectives of many African countries, as highlighted in their poverty reduction strategy papers (which serve as the basis for concessional loans and debt relief from the IMF, the World Bank, and other development partners), there is no doubt that high priority should be given to consolidating macroeconomic stability and strengthening competitiveness through sound fiscal, monetary, and exchange rate policies.

In this regard, *fiscal policy* will have a particularly important role to play. While ensuring financial stability, it should also be geared toward achieving higher growth rates and reducing poverty. Thus, in many cases, there will be a need to enhance tax efficiency and revenue collection through various reform measures, including reorienting the tax system from foreign trade taxes toward broad-based domestic consumption taxes, curbing tax exemptions, and strengthening revenue administrations. At the same time, it will be essential to reduce unproductive outlays (such as military spending and subsidies and transfers for inefficient public enterprises) and increase pro-poor spending, thereby improving the quality of public expenditure and reinforcing social cohesion. This reallocation of resources should be supported by a strengthening of expenditure-management systems, especially with a view to monitoring closely the delivery and impact of public services and social safety nets. Overall, however, government borrowing from the banking system should be strictly limited, if not eliminated, so as to provide greater scope for bank financing of the private sector and facilitate monetary management.

Concurrently, *monetary policy* should seek to contain the growth of the money supply to keep inflation in check. To this end, it would be desirable to rely increasingly on indirect instruments of monetary control, particularly open market operations, while ensuring that interest rates are freely determined by market forces.

As to the role of *exchange rate policy,* the shift toward increased exchange rate flexibility has led to the correction of fundamental misalignments in many African countries. Nevertheless, all countries will have to be mindful of the importance of sustaining competitive real exchange rates to facilitate their integration into the global economy, attract investment, and foster export diversification and growth.

Accelerating structural reforms

While promoting macroeconomic stability, African countries will need to accelerate structural reforms to remove impediments to investment and growth, as well as to reduce poverty and inequality. Although priorities will vary among countries, particular attention should be given to the following critical areas.

Investing in people and building capacity. In line with the international development goals, it will be important to boost basic education programs to achieve universal primary education and eliminate gender disparities in access to both primary and secondary education. But progress in education and training will also have to be broader and deeper to help sub-Saharan African countries bridge the digital divide, take full advantage of the vast knowledge available on the Internet, and improve their ability to compete on world markets. Similarly, intensified efforts should be made to expand health care services so as to reduce infant and child mortality rates as well as maternal mortality ratios. Most important, vigorous campaigns will be required to address the HIV/AIDS pandemic through comprehensive programs of prevention, care, and treatment.

Improving infrastructure and spurring agricultural development. In view of the major deficiencies in infrastructure, most countries will require substantial new investment in roads, ports, clean water, power, and telecommunications. Investment in transport facilities will be particularly important for landlocked countries that need to enhance their economic integration with other countries. It will also be necessary to transform agricultural practices and increase productivity for both food and export crops so as to achieve sustainable economic growth and poverty reduction.

Fostering trade liberalization and regional economic integration. Although significant progress was made in trade liberalization during the 1990s, sub-Saharan African countries need to open their economies more rapidly to the rest of the world, particularly by further simplifying and reducing their import tariff structures. They should also promote regional economic integration, in conjunction with market-oriented domestic policy reforms. If effectively implemented, this would allow countries to surmount the obstacles posed by their relatively small economies, enhance their ability to trade on a global basis, and help them attract needed capital.

Promoting a sound banking system and financial development. To this end, many countries will need to reinforce the prudential regulation and supervision of banks; recapitalize and restructure weak but financially viable institutions; improve loan recovery; promote international best practices and standards in bank management; and limit short-term foreign borrowing as well as modernize payments systems. Furthermore, it will be important to encourage the establishment of well-structured microfinance institutions that could offer needed savings and credit facilities, particularly for poor people in rural areas.

Encouraging private investment, including foreign direct investment that can bring added benefits through transfers of technology and know-how as well as increased access to international markets. The above-mentioned policies and reforms, together with the privatization of loss-making public enterprises, will greatly facilitate private investment, both domestic and foreign. But, above all, an enabling environment for private investment will require a credible regulatory framework and an evenhanded and efficient legal system that safeguards property rights, adequately enforces contracts, and protects healthy competition.

Promoting good governance in all its aspects. This is probably the most critical area of reform, as it would underpin and sustain the implementation of the entire country strategy for faster and more equitable growth. Good governance should start from the top, with the political leadership setting the best example by clearly demonstrating a firm commitment to responsible policies and practices. At the same time, this example should permeate all branches of the administration, the judiciary, and society at large to ensure that public sector and corporate operations are conducted in an irreproachable manner and all forms of corruption are shunned.

Need for international support

In sum, in the period ahead, sub-Saharan African countries will have to make much greater efforts to achieve sustainable economic and social progress. Although priorities will necessarily differ, there is no doubt that stronger macroeconomic policies and structural reforms, coupled with good governance in all its aspects, will be critically important. The region will also need peace and security to realize its development goals. Thus, urgent steps must be taken to prevent conflicts and resolve disputes promptly.

But, to have maximum impact and the best prospects for success, the reform programs of sub-Saharan African countries should be supported decisively by the international community in the context of a new partnership for development. Although several important initiatives have already been taken by industrial countries and multilateral institutions, including the IMF and the World Bank, these need to be broadened and deepened to ensure that all countries share the opportunities and benefits of globalization. The international community can make a vital contribution to Africa's progress by promoting steady, noninflationary growth in the world economy and strengthening the international financial architecture, thereby reducing the risks of major crises and destabilizing capital flows; actively supporting efforts to restore peace and security to war-torn countries; giving poor countries free access to industrial country markets, especially for agricultural products, textiles, and clothing, while starting a new, development-oriented trade round under the aegis of the World Trade Organization; providing deeper and faster debt relief to all eligible countries under the enhanced Heavily Indebted Poor Countries Initiative; and increasing substantially official development assistance in support of sound programs for reducing poverty and combating HIV/AIDS and other infectious diseases.

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